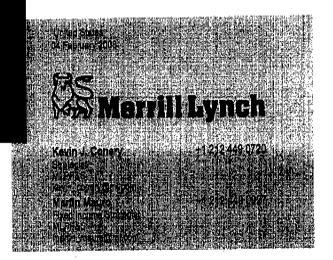
Auction Market Securities

Answering your questions about Auction Market Securities
We answer the questions that have come our way about Auction Market
Securities.



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Answering your questions about auction market securities

Are Closed-End Fund preferred auction securities safe? We consider CEF auction securities to be the conservative's conservative security. The fund and the fund manager must adhere to the provisions of the Investment Company Act of 1940.

- The fund is legally required to maintain the market value of the assets at a level equal to 200% of the face value of the auction market preferred. Typically, funds have asset coverage well above that threshold. Many funds maintain coverage levels at 300% or above. The preferred securities are the senior claim on the fund's assets.
- Under the regulations, funds are required to mark their assets to market every month. However, as a matter of good business practice, fund managers usually determine the market value either weekly or daily.
- If the fund is not able to meet the 200% asset coverage test, it must quickly remedy the situation. Historically, that has involved redeeming the security on the next auction date.
- Closed-end auction market preferreds have been around for 20 years. They
 have been through the S&L and banking crises of the late 1980s and early
 1990s, the Asian contagion, and the 2002 accounting scandals.

Can I be sure of getting my money back when I want it? Auction market securities do not provide the daily access to funds that money market funds do, but we think that the higher rates compensate for the slightly lesser degree of liquidity. Except in the rare case of a failed auction (see below), investors who choose to do so can receive their principal back at the next regularly scheduled auction. Depending upon the security, the auctions can reset at intervals of one week, one month, 49-days, or one quarter.

The rates on auction market securities seem too good to be true. What are we missing?

Rates on auction securities have been abnormally high in relation to other rates because of liquidity concerns, and in the case of some tax-exempt securities, concerns about the safety of the bond insurers. Liquidity concerns have been a common theme in the money markets since last summer.

We don't view the high spreads as a reason to worry. We are comfortable with the safety of auction securities from closed-end funds, municipals with an underlying credit rating of at least single-A, and Guaranteed Student Loan issuers. We view the unusually high present level of rates as an opportunity rather than a cause for alarm.

How likely is a default?

A default on an auction market security would mean that the security no longer pays interest or dividends. Defaults are even rarer than failed auctions. We are not aware of a default on an auction market security since the early 1990s. Given the high credit quality of the vast majority of the auction market, and the historical record, we believe a credit default on an auction market security is a very low probability.



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The Fixed Income Digest - Supplement

What is a failed auction?

A failed auction is one where there are more sellers than buyers, so that not all sellers can receive par value back. A failed auction is NOT a default.

In the event of a fail the investor can either: 1) liquidate the securities in the secondary market, but at a lower price than par, or 2) hold onto the security through subsequent auctions until an auction clears, the legal final maturity date, or when the issue is called. For the investor who holds on, the issuer will continue to pay interest on the security at a pre-determined higher maximum rate, as described in the issuer's prospectus. The rate is usually based on a markup above a designated market index. That rate is usually higher than the rate that would have cleared at the auction, and provides an incentive for the issuer to call the security.

How often do closed-end fund auctions fail?

Hardly ever. There was one failed auction on January 22, 2008. But that was an isolated event that involved only a small number of shares, and the next auction from that same closed-end fund was successful. Prior to the recent episode, the last failure that involved closed end fund securities held by individual investors was in 1990.

The auction failures in 1990 stemmed from the descent to insolvency of Drexel, Burnham, Lambert, who was the sole broker-dealer involved in the auctions. The fails lasted for several months until a new broker-dealer began supporting the auctions. Investors who held on did not lose money, as they received par value back when the auctions resumed with the new broker dealer.

What about the auction market securities backed by monoline insurers?

Although we don't expect the AAA-rated insurers to fail, we believe it is prudent for investors to evaluate insured securities on the basis of the underlying rating without the insurance. Most of the municipal bonds that are part of the auction market have a rating of A- or higher, and the monoline insurers follow a "zero loss" policy in insuring bonds. The historical default rate on investment grade municipal bonds is less than 0.1%, according to a Moody's report.

How do the relatively high auction market rate spreads affect the common shares of the closed-end funds?

Auction market rates have been higher than normal in relation to other rates, although the absolute level of rates has declined recently as the Fed has been cutting rates. To the extent that these rates remain high, they raise the costs of leverage for closed-end funds, and therefore hurt the earnings of the funds.

Analyst Certification

We, Martin Mauro and Kevin J. Conery, hereby certify that the views each of us has expressed in this research report accurately reflect each of our respective personal views about the subject securities and issuers. We also certify that no part of our respective compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.



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